

Decision 05-02-006 February 10, 2005

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

Application of Southern California Edison Company (U 338-E) for a Commission Finding that its Procurement-Related and Other Operations for the Recorded Period July 1 Through December 31, 2003 Complied with its Adopted Procurement Plan; for Verification of its Entries in the Energy Resource Recovery Account; for Recovery of a Nuclear Unit Incentive Reward of \$9.7 million; and for Recovery of \$4.9 Million Recorded in the Electric Energy Transaction Administration Memorandum Account.

Application 04-04-005  
(Filed April 1, 2004)

Robert Keeler, Attorney at Law, for Southern California Edison Company, applicant.

Regina DeAngelis, Attorney at Law, for the Office of Ratepayer Advocates.

**OPINION ON THE REASONABLENESS AND PRUDENCE  
OF SOUTHERN CALIFORNIA EDISON COMPANY'S  
ENERGY RESOURCE RECOVERY ACCOUNT**

**I. Summary**

We find that Southern California Edison Company's (SCE) administration of power purchase agreements and procurement of least cost dispatch power activities for the period beginning July 1, 2003 and ending December 31, 2003 (Record Period) were reasonable and prudent and that its procurement-related revenue and expenses recorded in its Energy Resource Recovery Account

(ERRA) for that Record Period resulting in a \$141 million ERRA overcollected balance at December 31, 2003 were reasonable and prudent. We also find that SCE's \$9.7 million Palo Verde Nuclear Unit Incentive Procedure (NUPR) reward amount and its \$4.9 million undercollected Electrical Energy Transaction Administration (EETA) Memorandum Account balance at May 21, 2003 were reasonable and recoverable. Finally, we defer a review of entries recorded in SCE's various generation and delivery service balancing accounts during the Record Period to SCE's April 1, 2005 ERRA reasonableness application.

## **II. Background**

Decision (D.) 02-10-062 established an ERRA balancing account for the major energy utilities to track fuel and purchased power revenues against actual recorded costs. That decision required the major energy utilities to establish an annual ERRA fuel and purchased power revenue requirement forecast and an annual ERRA reasonableness review through the application process.

An October 1<sup>st</sup> date was set for SCE's annual ERRA forecast application. However, that date was subsequently changed to August 1<sup>st</sup> pursuant to D.04-01-050. An April 1<sup>st</sup> date was set for SCE's annual ERRA reasonableness application. The purpose of that latter application, now before us, is to review the reasonableness of SCE's energy resource contract administration, least cost dispatch, and ERRA.

## **III. Contract Administration**

SCE's contract administration process consists of several activities, including exercising contract options in a prudent manner; verifying that the other party is complying with the contract terms, including credit support and collateral requirements; verifying that billing and payments are accurate and consistent with the terms of the contract; reviewing interruptions of service and

force majeure events; renegotiating contract provisions due to changed circumstances or conditions; resolving disputes; purchasing natural gas fuel under certain types of contracts; and assigning, renewing or terminating contracts.

The Office of Ratepayer Advocates (ORA) conducted an independent review and analysis of SCE's application, testimony, workpapers, data responses, and written description of SCE's contract administration procedures. Based on that review, ORA concluded that SCE's administration of its ERRA contracts was prudent and reasonable.<sup>1</sup> However, ORA did recommend that SCE include additional information in future ERRA applications to assist ORA's review of SCE's contract management activities. That additional information included copies of all amendments and modifications made to Qualifying Facilities' contracts and details of disputed settlement agreements.

At the evidentiary hearing, ORA acknowledged that the additional information could be provided through a master data request.<sup>2</sup> SCE concurred. Other methods available for ORA to obtain the additional information are through periodic data requests and through Pub. Util. Code §§ 581 through 584, which set forth procedures for a utility, such as SCE, to provide information to the Commission, of which ORA is a part.

Of those options available for ORA to obtain additional information, the data request option, whether it is through a master or periodic data requests, would provide ORA the flexibility to modify its informational needs as the

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<sup>1</sup> For standards of prudence adopted by the Commission see D.02-10-062; D.02-12-069; D.02-12-074; D.03-06-067; D.03-06-074; D.03-06-076; and D.03-12-003.

<sup>2</sup> Reporter's Transcript Vol. 1, p.61, lines 13 through 19.

circumstances warrant. In contrast, requiring the information as part of the application process would burden SCE with a requirement to provide substantial additional information (such as copies of all contract amendments and modifications) as part of all future application filings, irrespective of the relevance of such information to individual applications. For those reasons, we decline to require SCE to include the additional information requested by ORA as part of SCE's future ERRA applications.

ORA should utilize a data request process to obtain information not included in SCE's semi-annual ERRA applications, as the parties agree this is a viable alternative to request the additional information.

#### **IV. Least Cost Dispatch**

For SCE, the main goal of least cost dispatch is to determine the most economical generation schedule for SCE's own resources and dispatch contracts, taking into account potential spot trading opportunities at forecasted or observed energy and ancillary service market prices. Details of SCE's least cost dispatch are set forth in its testimony and exhibits.

ORA's independent examination of SCE's least cost dispatch consisted of a review of the application and prior commission decisions guiding the least cost dispatch process, meetings with SCE staff, and review of data responses. There was also a detailed demonstration of how SCE plans for least cost dispatch, daily resource plans, hourly and monthly hydro production for the Big Creek system, actual and day-ahead forecast load, and monthly spot sales and purchases. ORA's consultant, Electric Power Group (EPG), also reviewed SCE's least cost dispatch data and compared the mix of forward monthly sales versus sales in the hour-ahead and day-ahead markets to determine whether SCE used the most

cost-effective mix of total resources, including spot market transactions, to minimize its dispatch costs.

From that review and comparison of least cost dispatch activities ORA concluded that, with one exception, SCE had prudently performed its least cost dispatch activities during the Record Period. That exception pertained to an over reliance on day-ahead and hour-ahead markets (spot market) by SCE for its surplus energy sales. Based on a price differential between monthly sales and the spot market, ORA concluded that SCE unnecessarily incurred \$2.594 million in least cost dispatch cost during October and November of 2003 because SCE could have increased the amount of monthly sales and decreased spot sales during those months.

ORA recommended that SCE should investigate and report back to ORA whether its current forecasting methodology contains a bias toward underestimating daily peak loads. No action needs to be taken on the latter recommendation because SCE has agreed to conduct such an investigation and to report its result in SCE's forecast 2005 ERRA proceeding (A.04-08-008).

ORA also recommended that the least cost dispatch cost deemed unnecessary by ORA should be disallowed. However, that disallowance amount was based on incomplete information, as acknowledged by ORA,<sup>3</sup> and included many flaws, which were identified and addressed in the evidentiary record under seal. Those flaws included no allowance for SCE's decision to hold back some energy from the market to avoid the risk of having to buy that power back

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<sup>3</sup> Exhibit 5, p. 2-25.

at a premium if the actual load differed from anticipated energy supplies and a comparison between on-peak monthly prices to a mixture of spot prices.

ORA's recommended penalty for SCE's failure to increase its monthly sales over spot market sales during the months of September and October of 2003 is premature. Although SCE may have had the ability to increase its monthly sales during that time period, it is unclear whether such action would be prudent for SCE and its ratepayers. SCE should be provided a reasonable period of time to complete ORA's requested investigation to determine whether SCE's forecasting methodology includes a bias toward underestimating daily peak loads. If such a bias is found to exist, SCE should have an opportunity to mitigate that bias prior to imposing any penalty.

Absent evidence that demonstrates SCE unreasonably engaged in spot market transactions during October and November of 2003, the least cost dispatch disallowance recommended by ORA should be rejected and SCE's least cost dispatch activities within the Record Period should be found prudent.

#### **V. Energy Resource Recovery Account (ERRA)**

Consistent with D.03-07-029, SCE used its ERRA to record the difference between ERRA-related revenue and SCE's utility retained generation (URG) fuel costs and purchased power-related expenses during the Record Period. Department of Water Resources (DWR) power contract expenses were excluded from the ERRA. Details of its ERRA activity for the Record Period resulting in a \$140.5 million overcollected balance at December 31, 2003 were set forth in

Table XI-1 to its prepared testimony. SCE began to flow that overcollected ERRA balance back to ratepayers as of August 5, 2004.<sup>4</sup>

All parties, including ORA, agreed at the June 4, 2004 Prehearing Conference (PHC) that the scope of this proceeding would include a determination of the reasonableness of entries SCE recorded in its ERRA during the Record Period. All parties, including ORA, also agreed at that PHC that testimony from ORA and interested parties would be due on August 23, 2004 and that an evidentiary hearing would be held beginning September 21, 2004. No party requested an extension of time to participate in this proceeding.

However, ORA deferred unilaterally its review of SCE's ERRA and other balancing account entries recorded during the Record Period on the basis that it did not have the time or resources to review those entries.<sup>5</sup> ORA testified that it "**may**" review the ERRA and other balancing account entries recorded during the Record Period in an unspecified future ERRA proceeding.<sup>6</sup> Until such time that those entries are reviewed by ORA, ORA recommended that the rates "go into effect without the reasonableness of those balancing accounts."<sup>7</sup>

Although ORA did not specifically review each entry recorded in SCE's ERRA during the Record Period, ORA did scrutinize the source of those entries through its review of contract administration and least cost dispatch activities during the Record Period and did conclude that except for an over reliance on

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<sup>4</sup> Reporter's Transcript Vol. 1, p. 38.

<sup>5</sup> Exhibit 5, p. 1-2.

<sup>6</sup> Id.

<sup>7</sup> Reporter's Transcript Vol. 1, p. 65, lines 4 to 8.

the spot market, SCE had prudently performed its procurement related (contract administration and least cost dispatch) activities. ORA even recommended a specific disallowance for SCE's alleged over reliance on the spot market. Further, the Energy Division received and verified detailed ERRA monthly reports from SCE with supporting documentation for costs down to \$100.<sup>8</sup>

Based on ORA's conclusion that SCE had prudently performed its procurement related and least cost dispatch activities except for an alleged over-reliance on the spot market, the Energy Division's receipt and verification of ERRA monthly transactions down to \$100, and our review of SCE's detailed supporting ERRA information set forth in Exhibits 1 and 2, there is sufficient information to conclude that SCE's \$140.5 overcollected balance at December 31, 2003 and its procurement-related revenue and expenses recorded in its ERRA during the Record Period were reasonable and prudent.

#### **VI. Palo Verde Nuclear Unit Incentive Procedure (NUIP)**

The NUIP provides incentive rewards for those nuclear units that perform above an 80 percent capacity factor. If a reward is achieved, SCE's customers and shareholders share equally in the difference between the additional cost per kilowatt-hour (kWh) of nuclear fuel and the replacement power cost of the output above an that capacity factor. In D.01-09-041, the Commission capped the replacement power cost at five cents/kWh and extended the ratemaking mechanism for Palo Verde Units 1, 2, and 3 until the effective date of SCE's next GRC or further order of the Commission.

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<sup>8</sup> Id. p. 36.



The Palo Verde Unit 3 NUIP reward was an issue in SCE's 2003 ERRA reasonableness review because SCE and ORA differed on the kWh price that should be used to calculate the reward. SCE used the energy cap set in D.01-09-041 and ORA used California Independent System Operator's market clearing price as a reasonable proxy of the DWR then-actual prevailing market prices for incremental cost of energy.

Ordering Paragraph 3 of the decision issued in SCE's 2003 ERRA forecast proceeding (D.04-01-048) authorized SCE to include in its ERRA rewards associated with its Palo Verde Unit 3 subject to a DWR 2001-2002 energy cost true up in A.00-11-038 et. al. Pursuant to D.04-01-028, dated January 8, 2004, the energy cost was trued up to 8.649 cents per kWh. Because the 8.694 cents rate was also greater than the 5.000 cents per kWh cap set in D.01-09-048, the NUIP reward calculation does not differ from the amount calculated in D.04-01-048.

ORA reviewed SCE's NUIP reward calculation and concurred that the reward was properly calculated. Hence, the \$9.7 million NUIP reward applicable to SCE's Palo Verde Unit 3 was reasonable and is recoverable.

## **VII. Electric Energy Transaction Administration (EETA)**

EETA administrative and general costs are those costs incurred by SCE to procure, dispatch, settle, and administer procurement-related transactions. At May 21, 2003, SCE had a \$4.9 million undercollected balance in its EETAMA. Details of its activity in this mechanism for the period January 1, 2003 through May 21, 2003 were set forth in Table XV-1 of SCE's testimony.

SCE requested that the costs recorded in its EETA Memorandum Account (EETAMA) from January 1, 2003 through May 21, 2003 be found reasonable and transferred to its Base Revenue Requirement Balancing Account (BRRBA). The

BRRBA compares, on a monthly basis, the Commission-authorized distribution and generation base-related revenue requirements, including authorized EETA costs, with applicable retail revenues from distribution and generation base-related rates and includes distribution and generation sub-accounts to track over and undercollections.

ORA reviewed the EETAMA transaction during that time period and took no exception to those costs.<sup>9</sup> For that reason, SCE's EETA costs recorded in its EETAMA during the January 1, 2003 through May 21, 2003 period are found reasonable. SCE should be authorized to transfer its May 21, 2003 EETAMA undercollected balance of \$4.9 million to its BRRBA.

### **VIII. Other Balancing Accounts**

SCE also provided testimony on several other non-ERRA balancing account mechanisms. Those mechanisms were SCE's Electric Distribution Revenue Adjustment Balancing Account (EDRABA), Other Distribution Adjustment Mechanism (ODAM), Nuclear Decommissioning Adjustment Mechanism (NDAM), Public Purpose Programs Adjustment Mechanism (PPPAM), California Alternative Rates for Energy (CARE) Balancing Account (CBA), and Employee-Related Balancing Account (ERBA).

The following tabulation sets forth a summary of the individual balances and net balance of the balancing account mechanisms at the end of the Record Period. Details of its activities in the Record Period for those balancing account mechanisms were set forth in Tables XI 2 through 6 and Table XIII 1 of Exhibit 2.

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<sup>9</sup> Exhibit 5, p. 1-2.

<b>Mechanism</b>	<b>Millions Undercollected (Overcollected)</b>
EDRABA	\$(47.2)
ODAM	12.3
NDAM	2.6
PPPAM	(5.7)
CARE	43.1
ERBA	2.1
Net Balance Undercollected	\$ 7.2

SCE seeks a Commission finding that the entries recorded in those six ratemaking mechanisms for the Record Period were appropriate and correctly stated. However, none of those accounts were identified as an issue in the June 10, 2004 Assigned Commissioner's Scoping Memo and Ruling.<sup>10</sup> Further, ORA, the only other party to this proceeding, did not review or provide testimony on the reasonableness of those balancing account mechanisms.

With those balancing account mechanisms not identified as issues in the Scoping Memo and no party reviewing the reasonableness of those balancing account mechanisms, there is no basis to conclude that the entries recorded in those mechanisms during the Record Period were reasonable.

ORA did recommend in its opening brief that the Commission identify a separate proceeding for addressing the reasonableness of those balancing

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<sup>10</sup> Pub. Util. Code § 1701.1(b) requires the identification of issues to be considered in a proceeding and the applicable timetable for resolution of those issues to be included in a scoping memo.

account mechanisms. In that regard, official notice is taken of SCE's Advice Letter 1785-E that became effective on May 3, 2004, approximately one month after SCE filed this ERRA application. That Advice Letter provided for the above-identified balancing account mechanisms to be reviewed in SCE's annual April ERRA application. Consistent with SCE Tariffs, the reasonableness of the activities during the Record Period in above-identified balancing account mechanisms should be deferred to SCE's April 2005 ERRA application.

#### **IX. Confidential Information**

SCE tendered testimony as part of its reasonableness application to substantiate the prudence of its contract administration, least cost dispatch, and ERRA for the Record Period. Portions of SCE's data and testimony deemed commercially sensitive were tendered under seal, pursuant to General Order 66-C. Due to the commercially sensitive, confidential, and proprietary information on SCE's electric energy resources and its management of power resources to meet customers needs on a least cost basis, all such information deemed commercially sensitive was placed under seal pursuant to a May 5, 2004 Administrative Law Judge (ALJ) ruling.

Information placed under seal relates to certain purchased power contract terms and costs, individual power prices, net position cost assumptions and other information that might put SCE at a competitive disadvantage, if revealed. Maintaining this information under seal is reasonable and consistent with the provisions of Pub. Util. Code § 454.5(g), which states the Commission shall adopt appropriate procedures to ensure the confidentiality of any market sensitive information submitted in an electrical corporation's proposed procurement plan. Therefore, all such information placed under seal should remain under seal for a period of one-year from the effective date of this order except upon further order

or ruling of the Commission or ALJ then designated as the Law and Motion Judge.

#### **X. Procedural Matters**

SCE requested that this matter be categorized as ratesetting. By Resolution ALJ 176-3132, dated April 22, 2004, the Commission preliminarily determined that this was a ratesetting proceeding and that hearings may be necessary. There was no objection to the ratesetting categorization.

Notice of the application appeared in the Commission's Daily Calendar of April 8, 2004. An evidentiary hearing was held on September 21, 2004 and this matter was submitted upon the receipt of reply briefs on October 29, 2004.

#### **XI. Comment on Proposed Decision**

The proposed decision of the administrative law judge (ALJ) in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure. No comments were received.

#### **XII. Assignment of Proceeding**

Michael R. Peevey is the Assigned Commissioner and Michael J. Galvin is the assigned ALJ in this proceeding.

#### **Findings of Fact**

1. The application was filed on April 1, 2004, and appeared in the Commission's Daily Calendar on April 8, 2004.
2. SCE provided detailed exhibits and testimony on its administration of power purchase agreements, procurement of least cost dispatch power activities, and procurement-related revenue and expenses recorded in its ERRA for the Record Period beginning July 1, 2003 and ending December 31, 2003.

3. ORA provided testimony on the results of its independent examination of SCE's administration of power purchase agreements, procurement of least cost dispatch power activities, and ERRRA.

4. ORA and SCE concurred that additional ERRRA information could be made available through a data request procedure.

5. The reasonableness of entries recorded in SCE's ERRRA during the Record Period was an issue identified in the Assigned Commissioner's Scoping Memo.

6. No party requested an extension of time to participate in this proceeding.

7. ORA recommended a disallowance in SCE's least cost dispatch cost for excessive participation in the spot market based on incomplete information.

8. The Energy Division received and verified detailed ERRRA monthly reports from SCE with supporting documentation for costs down to \$100.

9. ORA scrutinized the source of entries recorded in SCE's ERRRA during the Record Period through its review of contract administration and least cost dispatch activities during the Record Period.

10. Exhibits 1 and 2 and Sealed Exhibits A, B, and C provided detailed support for transactions recorded in SCE's ERRRA during the Record Period.

11. NUIP provides incentive rewards for those nuclear units that perform above an 80 percent capacity factor.

12. ORA took no exception to SCE's Palo Verde Unit 3 NUIP reward calculation.

13. ORA took no exception to the costs recorded in SCE's EETAMA during the January 1, 2003 through May 21, 2003 period.

14. The Commission's Scoping Memo did not include various non-ERRRA balancing account mechanisms as issues in this proceeding.

15. ORA did not review the reasonableness on the various-non-ERRA balancing account mechanisms.

16. Official notice is taken of SCE's Advice Letter 1785-E that became effective on May 3, 2004.

17. Advice Letter 1785-E provides for the activities of various non-ERRA balancing account mechanisms to be reviewed in SCE's annual April ERRR application.

18. Information that would place SCE in a competitive disadvantage if disclosed was placed under seal.

### **Conclusions of Law**

1. SCE's administration of its ERRR contracts during the Record Period was reasonable and prudent.

2. There is no evidence that demonstrates that SCE unreasonably engaged in spot market transactions.

3. Least cost dispatch activities during the Record Period were prudently performed.

4. A procedure should be established for requesting and receiving additional ERRR information not included in SCE's ERRR applications.

5. The reasonableness of entries recorded in SCE's ERRR during the Record Period should be resolved in this proceeding.

6. SCE should be authorized to recover a \$9.7 million NUIP reward applicable to its Palo Verde Unit 3.

7. The May 21, 2003 EETAMA undercollected balance should be transferred to SCE's BRRBA.

8. Information placed under seal should remain sealed.

9. This decision should be effective today, in order to allow the docket to be closed expeditiously.

10. The reasonableness review of various non-ERRA balancing account mechanisms should be deferred.

## **O R D E R**

### **IT IS ORDERED** that:

1. Southern California Edison Company's (SCE) administration of its power purchase agreements and procurement of least cost dispatch power activities for the period beginning July 1, 2003 and ending December 31, 2003 were reasonable and prudent.

2. Working together, SCE and the Office of Ratepayer Advocates (ORA) shall establish a data request process that will allow ORA to timely request and receive additional ERRA information not included in SCE's ERRA applications.

3. SCE's \$141 million Energy Resource Recovery Account (ERRA) overcollected balance at December 31, 2003 and its procurement-related revenue and expenses recorded in its ERRA in that Record Period were reasonable and prudent.

4. A Nuclear Unit Incentive Procedure (NUIP) reward of \$9.7 million applicable to SCE's Palo Verde Unit 3 was reasonable and is recoverable.

5. Electric Energy Transaction Administration (EETA) costs recorded in SCE's EETA memorandum account during the January 1, 2003 through May 21, 2003 period resulting in a \$4.9 million undercollected balance was reasonable, the balance of which shall be transferred to its Base Revenue Requirement Balancing Account.



6. The reasonableness of 2003 activities in various balancing account mechanisms identified in the body of this order shall be reviewed as part of SCE's April 2005 ERRA application.

7. All information placed under seal shall remain sealed for a period of one year from the effective date of this order except upon further order or ruling of the Commission or Administrative Law Judge then designated as the Law and Motion Judge. If SCE believes that further protection of sealed information is needed beyond one year after the effective date of this order, it may file a motion stating the justification for further withholding of the sealed information from public inspection, or for such other relief as the Commission may provide. This

motion shall be filed no later than 30 days before the expiration of the one-year period specified in this ordering paragraph.

8. Application 04-04-005 is closed.

This order is effective today.

Dated February 10, 2005, at San Francisco, California.

MICHAEL R. PEEVEY  
President  
GEOFFREY F. BROWN  
SUSAN P. KENNEDY  
Commissioners

Comr. Grueneich recused herself  
from this agenda item and was not  
part of the quorum in its consideration.